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IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF CALIFORNIA
SAN JOSE DIVISION

THE BILLING RESOURCE d/b/a INTEGRETEL, Debtor-Plaintiff-Appellee, v. FEDERAL TRADE COMMISSION et al., Defendant-Appellant.	)	No. 5:07-CIV-5758-RMW

On Appeal from the United States Bankruptcy Court for the Northern District of California, No. 07-52890, Adversary Proceeding No. 07-5156 (Weissbrodt)

REVISED EXHIBIT 25 TO DEFENDANT-APPELLANT FEDERAL TRADE COMMISSION'S COMBINED MOTIONS FOR STAY PENDING APPEAL AND FOR CHANGE OF VENUE PURSUANT TO 28 U.S.C. § 1412

UNITED STATES BANKRUPTCY COURT

NORTHERN DISTRICT OF CALIFORNIA

In re: THE BILLING RESOURCE, dba INTEGRETEL, a California corporation, Debtor.	Case No. 07-52890-ASW Chapter 11
THE BILLING RESOURCE, dba INTEGRETEL, a California corporation, Plaintiff, vs. FEDERAL TRADE COMMISSION, et al., Defendants.	Adversary No. 07-5156

MEMORANDUM DECISION RE ORDER TO SHOW CAUSE REGARDING PRELIMINARY INJUNCTION

Before the Court is an Order to Show Cause ("OSC") why a preliminary injunction should not issue enjoining the Federal Trade Commission ("FTC") and David R. Chase ("Receiver"), not individually, but solely in his capacity as receiver for Access One Communications, Inc. ("Access One") and Network One Services, Inc. ("Network One")[1] from taking actions against The Billing Resource,

[1] In addition to these two entities, Receiver is also the receiver for several other entities in (continued...)

dba Integretel ("Integretel" or "Debtor")[2] in the action captioned Federal Trade Commission v. Nationwide Connections, Inc., et al., Case No. 06-80180-Civ-Ryskamp ("Florida Action") pending in the United States District Court for the Southern District of Florida ("Florida Court"). Debtor seeks to enjoin the FTC from prosecuting the enforcement aspect of the Florida Action ("Enforcement Action") against Debtor (and not against the other defendants in that action) as well as enjoining the Receiver from implementing or enforcing the Omnibus Order entered in the Florida Action on September 14, 2007 ("Omnibus Order") (as it relates solely to Debtor, and not to any other defendants). Debtor also seeks to unblock $1,762,762.56 currently held by Debtor in a blocked account ("Blocked Account"). These funds were taken from Debtor's general commingled funds and placed temporarily in the Blocked Account pursuant to a stipulation between Debtor and Receiver -- at the suggestion of the Court -- entered into at the September 26, 2007 hearing on Debtor's interim motion for use of cash collateral.

A hearing on the OSC was held on October 17, 2007 and the matter has been submitted for decision. Debtor is represented by Michael H. Ahrens, Esq. and Steven B. Sacks, Esq. of Sheppard, Mullin, Richter & Hampton, LLP. FTC is represented by Michael P. Mora, Esq. and Collot Guerard, Esq. Receiver is represented by Walter K. Oetzell, Esq. of Danning, Gill, Diamond & Kollitz, LLP and Jeffrey C. Schneider, Esq. of Tew Cardenas LLP. The Official

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[1](...continued)
the litigation brought by FTC in which Receiver was appointed. The only two receivership entities that are relevant to these proceedings are Access One and Network One.

[2] This Court will use Integretel to differentiate actions taken by or events related to Debtor that occurred pre-petition.

Committee of Unsecured Creditors ("Committee") is represented by John D. Fiero, Esq. of Pachulski Stang Ziehl & Jones LLP. Creditor POL, Inc. is represented by Kathryn S. Diemer, Esq. of Diemer, Whitman & Cardosi, LLP. Creditor PaymentOne Corporation ("PaymentOne") is represented by Stephen H. Warren, Esq. of O'Melveny & Myers LLP. Creditor United Online, Inc. is represented by Jeffrey K. Garfinkle, Esq. of Buchalter Nemer. BSG Billing Solutions is represented by James A. Pardo, Jr., Esq. and Felton E. Parrish, Esq. of King & Spalding LLP.

This Memorandum Decision constitutes the Court's findings of fact and conclusions of law, pursuant to Rule 7052 of the Federal Rules of Bankruptcy Procedure.

I.

FACTS

A. Debtor's Business[3]

Debtor provides billing-related and other services for smaller private telecommunications companies that compete with large local exchange carriers ("LECs") in niche areas such as public pay phones, hotels and prisons ("Alternative Operator Services"). Private telecommunications companies that provide Alternative Operator Services have difficulty billing for "collect" and other types of calls, since most individuals do not pay invoices from these unknown companies and those companies cannot bill the individuals through the individual's normal telephone bill. Debtor

[3] While "Debtor" refers to the post-petition business entity and "Integretel" refers to the pre-petition business entity, the Court uses Debtor in the following section rather than Integretel because the section describes Debtor's business both pre- and post-petition.

was created in 1988 to address this void in the marketplace. Debtor has billing and collection agreements with an estimated 1,400 LECs -- both major local exchange companies and numerous independents. Debtor's infrastructure permits private telecommunications providers to incorporate such providers' charges into the phone bills of more than 90% of business and residential consumers throughout the United States and Canada.

The typical service contract between Debtor and its service provider customers provides that the customer submits to Debtor the customer's billing transaction in a data format acceptable to Debtor. In the typical service contract, the customers acknowledge that these billing transactions are structured as a purchase of accounts receivable. Debtor contends that its customers have no ownership interest in the proceeds of the billing transaction after the billing transactions are submitted to Debtor and its customers hold only an unsecured claim against the distributions payable by Debtor to the customer under the service contracts -- usually in 90 or so days. The service contracts provide detailed formulas for computing the amounts Debtor owes to its customers. Debtor maintains certain reserves for disputes, fees and other adjustments as bookkeeping entries only.

The service contracts provide that each week Debtor transfer by wire to its customers' bank accounts the net proceeds identified in the prior week as defined by the service contracts. This amount is forwarded approximately 90 days after the submission of the billing transaction. Once Debtor receives a billing transaction, Debtor submits the billing information to the LECs and the LECs in turn bill the end user. At varying intervals, the LECs make

payments into Debtor's "wire in" account based on the billing transactions previously submitted to the LEC. Funds are transferred into this account every day throughout the day.

Once a week -- typically on a Thursday -- Debtor settles its accounts with its customers. To settle accounts, Debtor disburses funds from the "wire in" account to the "wire out" account. The "wire out" account is a zero balance account meaning that all funds transferred into that account are generally transferred out to several other accounts on the same day. It is from these other accounts that Debtor: (1) pays its vendors, employees and other operating expenses; (2) collects taxes that Debtor is required to collect in connection with Debtor's business; (3) makes payments to LEC end users that are entitled to a cash voucher for a refund;[4] and (4) holds excess funds, if any, from weekly settlements to cover subsequent operating shortfalls including settlement obligations that exceed available funds in the "wire in" account.

Debtor has approximately thirty-seven employees. In 2000, Debtor formed PaymentOne as a subsidiary to address the specialized billing and support requirements of the internet. Debtor owns 97% of PaymentOne. In 2002, Debtor formed another majority-owned subsidiary known as Inmate Calling Solutions, LLC to target the correctional industry and in 2004, Debtor formed yet another majority-owned subsidiary known as Information Services 900 LLC to target 900 call traffic.

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[4] Certain individual or business consumers are occasionally entitled to a refund or a credit. This results, inter alia, from an error in billing. Debtor asserts that 95% of these cases are corrected electronically through an automated credit transaction. In the 5% of errors handled through the issuance of a voucher to the consumer, the voucher -- redeemable for cash -- is drawn from the voucher account.

B. Florida Action

On February 27, 2006, the FTC commenced the Florida Action in the Florida Court against three Alternative Operator Services providers as well as their principals (not Integretel or its principals) for alleged deceptive and unfair practices for unauthorized billing of charges on phone bills in violation of the Federal Trade Commission Act. The FTC alleged that these defendants had defrauded consumers throughout the United States of more than $30 million by placing unauthorized collect call charges onto consumers' telephone bills. At the request of the FTC, the Florida Court entered an *ex parte* temporary restraining order ("TRO") that shut down the defendants' alleged unlawful operation, froze the defendants' personal and corporate assets and appointed Receiver as temporary receiver for the corporate defendants. Two of the corporate defendants -- Access One and Network One -- were prior customers of Integretel (collectively, "Prior Customers"). On March 8, 2006, a preliminary injunction was entered ("Preliminary Injunction") and Receiver was permanently appointed.

Both the TRO and the Preliminary Injunction provided, inter alia, that any business entity served with a copy of the TRO or Preliminary Injunction

> that holds, controls, or maintains custody of any account or asset of any Defendant, or has held, controlled or maintained custody of any such account or asset at any time since the date of entry of this Order, shall:
>
> A. Hold and retain within its control and prohibit the withdrawal, removal, assignment, transfer, pledge, encumbrance, disbursement, dissipation, conversion, sale, or other disposal of any such asset except by further order of the Court;
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> . . .

TRO at page 8; Preliminary Injunction at page 9. The FTC asserts that the FTC served Integretel with the TRO within days of the entry of the TRO.

On March 6, 2006, Integretel's president, Ken Dawson, submitted a letter to the FTC stating in relevant part that: (a) Integretel had service contracts with the Prior Customers; (b) pursuant to the service contract with the respective Prior Customer, each Prior Customer was entitled to certain proceeds from billing transactions; however (c) each Prior Customer was in default under the service contract and no amounts were currently due and owing. Mr. Dawson noted that Integretel had not processed any billing for Access One since May 2005 nor for Network One since June 2003. With respect to each Prior Customer, Mr. Dawson stated: "[t]o the extent proceeds become due to [Prior Customer] in the future, we will establish a separate bank account into which such funds will be deposited and notify your office accordingly."[5] Pre-petition Integretel did not establish any such separate bank account.

On September 21, 2006, the FTC filed an amended complaint asserting claims against Integretel for Integretel's collection of alleged fraudulent charges. Specifically, the complaint asserts that Integretel deceptively billed consumers for collect calls that were never made, received or authorized. In its complaint, the FTC seeks a monetary judgment as well as multiple forms of non-monetary relief such as a permanent injunction against pertinent law

[5] Letter dated March 6, 2006 from Ken Dawson to Roberto Menjivar, Attachment B to Declaration of Laura Kim in Opposition to Plaintiff's Motion for a Temporary Restraining Order and Preliminary Injunction filed on October 1, 2007.

violations, "fencing-in" injunctive relief, rescission of contracts and a claims procedure for consumer redress. Integretel filed an answer denying the FTC's allegations. Integretel's principals were not named in the amended complaint.

On October 16, 2006, Receiver filed a motion in the Florida Court seeking to hold Integretel in contempt of court for Integretel's alleged failure to turn over to the Receiver on behalf of the Prior Customers certain "reserves" under the service contracts with the Prior Customers in an alleged amount in excess of $1.4 million. Integretel opposed the motion on various grounds, including: (a) Integretel did not hold any such reserves in a separate account; (b) the service contracts in place with the Prior Customers permitted Integretel to withhold certain monies owed to the Prior Customers as "reserves"; and (c) Integretel was not obligated to turn over those funds under the respective service contracts. Integretel also filed its own motions to modify the Florida Court's injunctive orders and to stay the contract claims pending arbitration. A hearing on these motions was held on April 12, 2007.

On September 14, 2007, the Florida Court entered the Omnibus Order. In the Omnibus Order, the Florida Court found that Integretel held reserves in the amount of $1,762,762.56 on behalf of the Prior Customers as of June 30, 2007 ("Commingled Funds"). The Florida Court stated that Integretel's assertion that the "reserves" were not held as segregated funds but rather were kept in a pooled account and tracked via an internal accounting entry was "a distinction without a difference, since the TRO captures funds 'held on behalf of, or for the benefit of, a Defendant.'"

Omnibus Order at 3. The Florida Court noted that "[a]n entity need not be an agent, partner, joint venturer, trustee, fiduciary, or legal representative to possess funds that one is holding 'on behalf of' another person or entity..." Id. The Florida Court also rejected Integretel's arguments that Integretel could retain the "Commingled Funds" to fund Integretel's assertion of an indemnity claim or liquidated damages for breach of contract against the Prior Customers. Id. at 4.

Regarding Integretel's motions, the Florida Court denied Integretel's request to stay the contract claims pending arbitration of those claims pursuant to the service contract arbitration clause, since the Florida Court concluded that Receiver was not bound by the those clauses. The Florida Court stated in particular:

> The Receiver's claim is not a claim at law governed by pre-receivership contracts, however, but one governed by this Court's jurisdiction over receivership property based on the TRO and Amended Preliminary Injunction. The Receiver does not claim that the funds must be turned over according to, or by adopting, a contract signed between Integretel and Access One/Network One. The Receiver is seeking to recover the reserve funds pursuant to the Court's in rem jurisdiction over receivership property, as memorialized in the TRO and the Amended Preliminary Injunction.

Omnibus Order at 4. In response to Integretel's argument that the TRO and Preliminary Injunction would be invalid if those orders permitted the Florida Court to determine Integretel's ownership interest -- or lack thereof -- in the Commingled Funds without a new, separate legal proceeding, the Florida Court stated: "[i]ssues concerning entitlement to disputed receivership property, in fact, are the types of issues typically determined via summary proceedings in the federal court equity receivership context."

Id. at 5. The Florida Court rejected Integretel's arguments that Integretel was deprived of due process when the Florida Court issued the TRO and Preliminary Injunction and also rejected Integretel's various arguments that those orders are invalid. The Florida Court also denied Integretel's request to modify those orders. Finally the Florida Court:

> ORDERED AND ADJUDGED that the Receiver's Revised Motion for Order to Show Cause Why Integretel Should Not Be Held in Contempt of Court, filed October 16, 2006 **[DE 246]**, is GRANTED. Integretel shall show cause in writing within 10 days of the date of this Order why it should not be held in contempt for failure to turn over the reserves. In addition, Integretel shall provide a sworn statement identifying the amount of reserves as of the issuance of the TRO. The Court further orders that these funds shall be placed in a segregated Receivership account. It is further
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> ORDERED AND ADJUDGED that Integretel's Motion to Modify Prior Injunctive Orders, filed October 30, 2006 **[DE 294]**, is DENIED. It is further
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> ORDERED AND ADJUDGED that Integretel's Motion to Stay Contract Claims, filed December 29, 2006 **[DE 363]**, is DENIED. . . .

Omnibus Order at 10. On September 16, 2007, promptly after receiving the Omnibus Order, Integretel filed its bankruptcy petition.

Debtor is one of seventeen defendants in the Florida Action. Other than two pending motions regarding depositions, discovery is complete in the Enforcement Action.[6] Dispositive motions are scheduled to be filed very soon -- by November 6, 2007, with opposition to those motions to be filed by December 4, 2007, and replies due by December 18, 2007. Debtor asserts that Debtor will

[6] Integretel filed a motion to continue one deposition and another billing aggregator defendant filed a motion requesting ten additional depositions. The FTC opposed both motions and the Florida Court had not ruled on those motions as of October 15, 2007.

not be filing any dispositive motions, but anticipates having to respond to dispositive motions filed by other parties. The FTC has stated that the FTC will seek summary judgment against Debtor. Debtor asserts that a two- to four-week trial is set to commence in the Florida Action on February 25, 2008. The FTC predicts that the FTC will prevail on the liability aspect in summary judgment and if not, the FTC estimates that the trial will be no more than nine days, and other defendants contend that the trial will take ten to fifteen days at most. The FTC does not contend that a preliminary injunction against Debtor interferes with the FTC from proceeding with the Enforcement Action against any of the other sixteen defendants.

Debtor anticipates having to spend $821,600 in litigation costs over the next six months related to depositions, discovery motions, dispositive motions, other motions, pre-trial submissions and trial.[7] Debtor does not break out the estimated fees into the various subcategories. Debtor estimates that in addition to those fees there will be an estimated $10,000 in fees for local counsel and an estimated $50,000 to $75,000 in costs.[8] In addition to these estimated fees and costs, Debtor estimates that Debtor will incur an additional $50,000 to $150,000 in fees related to Receiver's request for turnover of the Commingled Funds.[9]

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[7] Declaration of Neal Goldfarb in Support of Emergency Motion for Temporary Restraining Order and Preliminary Injunction filed on September 24, 2007 ("Goldfarb Dec.") at ¶¶ 5-6.

[8] Goldfarb Dec. at ¶ 7.

[9] Goldfarb Dec. at ¶ 8.

C. Events since Debtor Filed Its Bankruptcy Petition

As noted above, Debtor filed this chapter 11 bankruptcy case on September 16, 2007. On September 17, 2007, Debtor filed a Notice of Bankruptcy in the Florida Action. On September 18, 2007, this Court generated a Notice of Chapter 11 Bankruptcy Case, Meeting of Creditors, & Deadlines setting, inter alia, a meeting of creditors for October 17, 2007 and a deadline for filing a proof of claim for non-governmental units of January 15, 2008 and for governmental units of March 14, 2008. On September 20, 2007, the Florida Court issued an order stating that the Florida Action was stayed by the automatic stay.

On September 21, 2007, the FTC filed an emergency motion for clarification that the automatic stay did not apply to the Enforcement Action and the contempt proceedings. On the same day, without granting Debtor an opportunity to respond to the FTC's emergency motion either in writing or orally, the Florida Court issued its Order Granting Motion for Clarification as to Scope of Stay ("Clarification Order"). In the Clarification Order, the Florida Court stated that in the Omnibus Order the Florida Court had "ruled that the reserve funds are the property of the receivership estate and ordered Integretel to pay the current reserve funds, amounting to $1,762,762.56, immediately to the Receiver." Clarification Order at 1.

Furthermore, the Florida Court held that Bankruptcy Code section 362(b)(4)[10] did not stay the Enforcement Action. The

[10] Unless otherwise noted, all statutory references are to Title 11, United States Code, as amended in 2005 ("Bankruptcy Code").

Florida Court also stated with respect to the contempt proceedings brought by the Receiver:

> Nor is the contempt proceeding stayed. First, the automatic stay applies only to protect property of the bankruptcy estate or property of the debtor. See 11 U.S.C. § 362(a)(2). The Court has already ruled that the reserve funds are neither the property of the "bankruptcy estate" nor Integretel. Second, the 11 U.S.C. § 362(b)(4) exception also applies to civil contempt proceedings brought by a governmental unit in the exercise of its police or regulatory powers. See SEC v. Bilzerian, 131 F. Supp. 2d 10, 14 (D.D.C. 2001)(civil contempt proceeding falls within the exception; incarceration of debtor subsequent to failure to provide financial information as required by purgation provision in prior disgorgement order). Finally, the bankruptcy filing does not deprive this Court of its inherent power to enforce the integrity of its orders. "[C]ontempt orders to uphold the dignity of the court are excepted from the automatic stay." NRLB v. Sawulski, 158 B.R. 971, 975 (E.D. Mich. 1993).

Clarification Order at 4. Thus, even though the newly extant bankruptcy estate had no opportunity to respond to the FTC's emergency motion, the Florida Court granted the FTC's emergency motion. The Florida Court stated that the commencement of Debtor's bankruptcy case did not stay the contempt proceedings against Debtor or FTC's prosecution of the Enforcement Action and the Florida Court vacated the September 20, 2007 order staying proceedings against Debtor.

Also on September 21, 2007, this Court held a hearing on Debtor's emergency motion for interim use of cash collateral and Debtor's request for authority to maintain Debtor's pre-petition bank accounts. In its motion for interim use of cash collateral, Debtor requested court authority to use cash collateral pursuant to a stipulation with its secured creditor PaymentOne. Debtor asserted that PaymentOne was a secured creditor based on more than $6.4 million PaymentOne had loaned to Debtor between October 18,

2006 and the petition date (the "new value" provided by PaymentOne, in bankruptcy parlance). The motion for authority to maintain Debtor's pre-petition bank accounts was granted and the motion on the interim use of cash collateral was continued to September 26, 2007.

Prior to the September 26, 2007 hearing, seven objections were filed in opposition to Debtor's motion for interim use of cash collateral. Some of the oppositions raised questions regarding Debtor's viability and ability to operate successfully as a going concern. Prior to and at the hearing, Debtor obtained the consent of all parties to Debtor's use of cash collateral. In particular, Debtor and Receiver agreed to set up the Blocked Account whereby Debtor agreed to deposit $1,762,762.56 of its commingled funds into a blocked account and Debtor and Receiver agreed that the establishment of the Blocked Account did not in any way affect the merits of either parties' rights, claims or defenses with respect to the funds in the Blocked Account. Based in part on the consent of all parties, this Court granted Debtor interim use of cash collateral through October 15, 2007 and set a further hearing on the use of cash collateral for that day.

In papers relating to the September 26, 2007 hearing and at that hearing, Debtor informed this Court that negotiations were underway for a possible sale of PaymentOne to a third party. Debtor also requested the expedited appointment of the unsecured creditors' committee so that Debtor would have an entity with which Debtor could talk on a confidential basis with, and obtain the opinions regarding, possible reorganization scenarios, including the possible sale of PaymentOne. On October 1, 2007, the United

States Trustee filed a notice that a committee of seven unsecured creditors of Debtor had been appointed. Two days later the Committee selected the law firm of Pachulski Stang Ziehl & Jones LLP as its counsel, subject to approval of this Court. Within a week, Debtor and the Committee executed a confidentiality agreement; Debtor provided the Committee with various documents and information requested by the Committee; and the Committee began the process of analyzing that information.

On October 10, 2007, the Committee and Debtor participated in a five hour face-to-face meeting. Discussions at that meeting included Debtor's financial information -- including projections, claims against Debtor, Debtor's plan for post-petition pre-payment to Debtor's pre-petition customers, Debtor's relationship with the LECs, the status of the Florida Action, as well as plan of reorganization issues. At that meeting, the Committee agreed to consent to Debtor's continued use of cash collateral through November 2. Debtor committed to negotiate with the Committee a term sheet for a plan of reorganization contemplating a continuation of Debtor's business operations with the goal of allowing Debtor to exit bankruptcy as quickly as possible, while maximizing the value to unsecured creditors. The Committee stated its intention to use the time between October 10 and November 2 to conduct further due diligence on Debtor's assets, liabilities and financial affairs in an effort to be in a better position to evaluate an exit strategy for Debtor from bankruptcy.

On October 15, 2007, this Court held a second hearing on Debtor's interim use of cash collateral. In support of Debtor's continued use of such cash collateral, Debtor submitted budgets

showing Debtor's actual and projected post-petition finances. Debtor submitted one budget assuming that Debtor could use the funds in the Blocked Account as well as the assumption that the Enforcement Action and related proceedings were stayed. Debtor also submitted another budget without those assumptions. Regarding the projected $1 million in litigation expenses related to the Florida Action, Debtor projected incurring $333,333 for the weeks ending November 2, 2007, December 7, 2007, and January 4, 2008. Debtor asserted at that hearing, and continues to assert, that Debtor needs the funds in the Blocked Account and that without the ability to use the funds in the Blocked Account, Debtor will not have sufficient cash flow as of mid-December 2007.

Debtor's continued use of cash collateral again drew seven objections, but the primary concern of the objecting creditors was with respect to the alleged secured nature of their respective claims, and not on Debtor's ability to stay in business. In addition, as noted above, Debtor's continued use of cash collateral had the support of the Committee. On October 16, 2007, this Court granted Debtor's continued interim use of cash collateral. A hearing for final authority for Debtor to use cash collateral is set for November 2, 2007.

Meanwhile, on October 1, 2007, Debtor requested additional time -- until November 15, 2007 -- to file its schedules of assets and liabilities ("Schedules") and statement of financial affairs ("Statement"). In its application, Debtor noted the size and complexity of Debtor's business operations, coupled with the limited number of employees, who, in addition to their regular duties, were capable of preparing the Statement and Schedules. On

October 23, 2007, this Court granted Debtor's request. Debtor's Schedules and Statement are currently due on November 15, 2007.

On October 2, 2007, Debtor sought a temporary restraining order from this Court enjoining the Enforcement Action and seeking an order to show cause for the issuance of a preliminary injunction. At that hearing, this Court denied Debtor's request for a temporary restraining order of the Enforcement Action on the basis that for the period from October 2, 2007 through October 17, 2007, Debtor had not demonstrated that the threatened injury to Debtor outweighed the harms of a temporary restraining order against the FTC.[11] However, the Court found that there was cause to issue the OSC and the OSC was issued as to why a preliminary injunction should not issue.

On October 11, 2007, Debtor filed in the Eleventh Circuit a motion for an immediate interim stay of the Clarification Order in as far as that order held that the Florida Action -- other than the Enforcement Action -- was not automatically stayed. On October 17, 2007, the Eleventh Circuit temporarily granted Debtor's motion pending further order of the court ("Stay Order").

II.

APPLICABLE LAW

> In the non-bankruptcy context, [the Ninth Circuit has] consistently required trial courts deciding preliminary injunction motions to balance the moving party's likelihood of success on the merits and the

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[11] While Debtor originally sought a temporary restraining order against Receiver's continued enforcement of the Omnibus Order, the stipulation at the September 26 cash collateral hearing that resulted in the temporary establishment of the Blocked Account resolved that need to both parties' satisfaction.

relative hardship of the parties. The moving party must show:

> (1) a strong likelihood of success on the merits, (2) the possibility of irreparable injury to plaintiff if preliminary relief is not granted, (3) a balance of hardships favoring the plaintiff, and (4) advancement of the public interest (in certain cases). Alternatively, a court may grant the injunction if the plaintiff demonstrates *either* a combination of probable success on the merits and the possibility of irreparable injury *or* that serious questions are raised and the balance of hardships tips sharply in his favor.
>
> As we have said many times regarding the two alternative formulations of the preliminary injunction test: These two formulations represent two points on a sliding scale in which the required degree of irreparable harm increases as the probability of success decreases. They are not separate tests but rather outer reaches of a single continuum.

Save Our Sonoran, Inc. v. Flowers, 408 F.3d 1113, 1120 (9th Cir. 2005) (citations and internal quotation marks omitted).

Solidus Networks, Inc. v. Excel Innovations, Inc., (In re Excel Innovations, Inc.), --- F.3d ---, 2007 WL 2555941 at *5 (9th Cir. Sept. 7, 2007) (emphasis in original). The usual preliminary injunction standard applies to stays of proceedings under 11 U.S.C. § 105(a) ("Section 105"). Excel, 2007 WL 2555941 at *7. In Excel, a reorganization case, the Ninth Circuit stated that in granting or denying an injunction under Section 105, "a bankruptcy court must consider whether the debtor has a reasonable likelihood of a successful reorganization, the relative hardship of the parties, and any public interest concerns if relevant." Excel, 2007 WL 2555941 at *7.

III.

ANALYSIS

A. Reasonable Likelihood of a Successful Reorganization

In a reorganization context, a debtor seeking a stay against a non-debtor must show a reasonable likelihood of a successful reorganization. Excel, 2007 WL 2555941 at *7. This is not a high burden, id. at *8, and a strong showing on the likelihood of a successful reorganization lowers the burden to show irreparable harm. Id. at *11.

The FTC argues that the Committee's unwillingness to consent to a final cash collateral order speaks volumes about Debtor's prospects -- or lack thereof -- of successfully reorganizing and that it remains to be seen whether this will be a "real" reorganization case. Citing general statistics, the FTC asserts it is more likely that Debtor's case will fall into the 90% or more of chapter 11 cases that are converted to liquidations or dismissed. The FTC argues that overall the record at this point demonstrates that Debtor's fate hangs precariously in the balance and a liquidation scenario is more, or at least as likely as, a successful reorganization and Debtor has not shown by a preponderance of the evidence a likelihood of success on the merits.[12]

Receiver asserts that Debtor has not shown a likelihood of success on the merits on the basis that Debtor's support by the Committee fails to address the numerous objections by creditors

[12] A bankruptcy case may have an excellent result for creditors, even in a liquidation context. For example, a successful sale of a debtor's business and subsequent liquidation of that debtor's assets in a chapter 11 or a chapter 7 may result in a substantial distribution to creditors.

claiming a security interest in Debtor's assets to Debtor's continued use of cash collateral. In addition, Debtor's strategy over the near-term presupposes Debtor will be able to use the Commingled Funds to fund Debtor's business operations, so Debtor cannot show a likelihood of success on the merits.

The Court disagrees with the FTC and Receiver. The Court finds that, at this juncture, Debtor has made a strong showing that Debtor has a reasonable likelihood of a successful reorganization. It is very early in Debtor's bankruptcy case -- Debtor's bankruptcy case is only six weeks old. In that short period of time, Debtor has obtained the confidence of its creditors that Debtor is a viable business and has a reasonable likelihood of reorganizing successfully. This is demonstrated in several ways. First, following strenuous initial objections, Debtor's creditors consented to Debtor's first interim use of cash collateral as soon as Debtor demonstrated its viability to the objecting creditors. Second, the LECs have for the most part continued to forward funds to Debtor. Third, in an effort to retain customers, Debtor is negotiating with its customers to provide a 50% pre-payment of the transferred accounts receivables at the time of transfer rather than having the customers wait 90 days, as those customers did pre-petition. Debtor has obtained the Committee's support of that plan. Fourth, the Committee is confident enough in Debtor's prospects of reorganization that the Committee supported Debtor's continued use of cash collateral for an additional three weeks to enable the Committee and Debtor to work together on the terms of a plan of reorganization.

In addition, Debtor and Debtor's 97%-owned subsidiary PaymentOne are diligently exploring both a reorganization with Debtor and a sale of PaymentOne's business to prospective purchasers. The proceeds of such a sale could help Debtor fund a plan of reorganization. Alternatively, Debtor is exploring the possibility of a pot plan providing a pro-rata distribution to unsecured creditors or a plan that would have Debtor continue its operations and issue new stock in exchange for Debtor's unsecured debt.

At this early stage of Debtor's bankruptcy case, Debtor's reasonable likelihood of a successful reorganization is evident from the support of Debtor's creditors and the Committee, Debtor's clear pursuit of several viable avenues of possible reorganization, Debtor's projections of positive cash flow for the next six months, Debtor's retention of its customers and the continued success of Debtor's business. Thus, Debtor has met its burden of showing a reasonable likelihood of a successful reorganization.[13]

B. The FTC's Enforcement Action

The parties do not dispute for the purposes of the current dispute that, under Bankruptcy Code section 362(b)(4), the automatic stay does not stay the Enforcement Action.[14] However, the

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[13] Although the issue is not presented here, a court might appropriately enjoin an enforcement action, like the FTC's, against a chapter 7 estate. The chapter 7 trustee might well convince the court not to allow the enforcement action to proceed until the trustee and the court knew what assets and liabilities there were in the estate. There would be no point, for example, in allowing an enforcement action seeking a monetary judgment to proceed if the estate did not have any money in it above the amount needed to pay administrative claims. There also might be no purpose in enjoining a chapter 7 debtor from engaging in certain business practices, if that debtor was out of business.

[14] While the Clarification Order in which the District Court held that Bankruptcy Code

(continued...)

FTC argues that this Court does not have authority to stay that litigation against Debtor under Section 105. This Court disagrees. Under In re First Alliance Mortg. Co., 264 B.R. 634 (C.D. Cal. 2001) ("FAMCO") and the myriad of authorities cited therein, this Court has the legal authority to enjoin prosecution of governmental actions against a debtor that falls within the regulatory and police powers exception of Bankruptcy Code section 362(b)(4). FAMCO, 264 B.R. at 652 n.18.

This Court may enjoin the prosecution of the Enforcement Action under Section 105 if the Enforcement Action "threatens" the assets of the bankruptcy estate. FAMCO, 264 B.R. at 652. Under FAMCO, a Section 105 injunction could be appropriate against a regulatory action in two types of situations.

> First, a governmental action that seeks actual physical control over the assets of the debtor's estate threatens the bankruptcy court's exclusive jurisdiction over the *res* of the debtor's estate and therefore can be enjoined. . . .
>
> Second, a § 105 injunction of a regulatory or police powers action could be appropriate in other circumstances that severely threaten the integrity of the bankruptcy process. A few courts have enjoined regulatory or police powers actions on the grounds that the costs of defending the actions at issue, both in terms of money spent on lawyers' fees and time taken away from focusing on reorganization, were so high in comparison to the assets of the estate that allowing the actions to continue constituted a "threat" to the estate. E.g., NLRB v. Superior Forwarding, Inc., 762 F.2d 695, 698-99 (8th Cir. 1985). Because the bankruptcy court has the obligation to protect and marshal the estate's assets, a severe enough threat to the assets of the estate constitutes a threat to the bankruptcy process.

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[14](...continued)
section 362(b)(4) did not apply to the Florida Action is on appeal, in that appeal, Debtor has not challenged that Order insofar as the Clarification Order holds that the Enforcement Action is not automatically stayed.

Id. at 655. In balancing the hardships between the parties, "[a] bankruptcy court must 'identify the harms which a preliminary injunction might cause to defendants and ... weigh these against plaintiff's threatened injury.' Caribbean Marine Servs. Co. v. Baldridge, 844 F.2d 668, 676 (9th Cir. 1988)(citation omitted)." Excel, 2007 WL 2555941 at *9.

1. Harms to FTC

The FTC articulates that the FTC would be harmed by the granting of a preliminary injunction because the FTC only seeks what the FTC terms as "equitable" relief in the Enforcement Action and this Court cannot grant all of the relief requested by the FTC.[15] But there is no doubt that the FTC seeks to collect monies from Debtor. Specifically, the FTC seeks monetary injunctive relief in the form of disgorgement of monies received from consumers and restitution to the consumers. In addition, the FTC seeks a permanent injunction halting Debtor's allegedly unlawful practices, rescission of contracts and a claims procedure to provide restitution to the consumers who allegedly paid for unauthorized charges on their phone bills.

The FTC also asserts that being enjoined from proceeding in its chosen forum -- the Florida Court -- would harm the FTC in other critical ways. The FTC quotes extensively from FAMCO which states in this regard:

> [T]he hardship to the governmental units of not being allowed to proceed with their actions in their chosen forums includes harms different in character from the

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[15] While this Court does not necessarily agree with the FTC that this Court could not grant all equitable relief requested by the FTC in the Enforcement Action, due to the limited nature of the preliminary injunction being granted at this time, there is no reason for this Court to address the FTC's assertion.

> harms normally considered on motions for injunctions under § 105. Being able to have a claim determined by the bankruptcy court is qualitatively different from proceeding with a lawsuit in home forums. As Congress recognized when it created the regulatory and police powers exception, the goals of public policy, punishment, and deterrence may sometimes conflict with the goals of maximizing an individual estate's assets and efficiently processing claims. It is the former goals, which are difficult if not impossible to measure in dollars and cents, that are impaired when a governmental unit loses the ability to enforce its laws in its own forum.
>
> Considering deterrence in particular, the harm to the governmental units must be measured with a broader perspective in mind than these parties alone. The bankruptcy court and First Alliance are undoubtedly correct that there will be more money to distribute to borrowers in this case if the separate actions are not allowed to proceed. However, the governmental units are entitled to make the choice that, over time, similarly situated borrowers and consumers benefit more when companies do not violate the law in part because they know that bankruptcy will not provide a way out when their wrongs are discovered. In any given case, reasonable minds could disagree about the marginal costs and the marginal benefits of different approaches and which will maximize the wealth and happiness of the greatest number of people. The point is that it is the governmental units charged with enforcing consumer protection laws, governmental units that are responsive to the political will of the people, that should be the ones to make the choice, not the bankruptcy court.

FAMCO, 264 B.R. at 659.

The FTC asserts that the FTC's need for permanent injunctive relief is particularly acute here because the FTC needs permanent injunctive relief from the Florida Court barring Debtor's allegedly unlawful business practices. The FTC asserts that the FTC's pursuit of phone billing aggregators such as Debtor is a vital enforcement strategy that the FTC has pursued to curb the allegedly insidious and unlawful practice of placing unauthorized charges on consumers' phone bills. During the past nine years, the FTC has filed numerous actions against telephone billing aggregators and has obtained injunctive and monetary equitable relief. The FTC

notes that this is not the first time that the FTC has sued Debtor (the previous suit was settled) and some of Debtor's current customers were recently prosecuted by state attorneys general for placing unauthorized charges on consumers' phone bills and other alleged deceptive trade practices.

2. Harms to Debtor

Debtor has filed a chapter 11 bankruptcy petition. "The purpose of title 11 protection is to allow an entity to 'restructure ... finances' and enter a plan of reorganization so that it is able to 'continue to operate, provide its employees with jobs, pay its creditors, and produce a fair return for its stockholders.'" CFTC v. NRG Energy, Inc., 457 F.3d 776, 779 (8th Cir. 2006) (internal citation omitted). Said a different way, "[t]he purpose of Chapter 11 reorganization is to assist financially distressed business enterprises by providing them with breathing space in which to return to a viable state." In re Little Creek Dev. Co., 779 F.2d 1068, 1073 (5th Cir. 1986) (quoting In re Winshall Settlor's Trust, 785 F.2d 1136, 1137 (6th Cir. 1985)). Here "Debtor 'is a real company with real debt, real creditors and a compelling need to reorganize in order to meet these obligations' and is therefore, exactly the type of debtor for which chapter 11 was enacted." In re Dow Corning Corp., 244 B.R. 673, 677 (Bankr. E.D. Mich. 1999), aff'd, 255 B.R. 445 (E.D. Mich. 2000) (internal citation omitted). In determining irreparable injury to Debtor, this Court must consider the impact of permitting the Enforcement Action to proceed against Debtor at this point in Debtor's bankruptcy case.

Debtor raises two main harms that would cause irreparable injury should this Court not preliminarily enjoin the Enforcement Action. First, Debtor anticipates having to spend over $900,000 in fees and costs over the next six months in the Enforcement Action. Debtor estimates it will incur $821,600 in litigation fees related to depositions, discovery motions, dispositive motions, other motions, pre-trial submissions and trial. In addition, Debtor estimates that there will be an estimated $10,000 in fees for local counsel and an estimated $50,000 to $70,000 in costs. Debtor's budgets show that Debtor will not be able to operate on an administratively solvent[16] basis if Debtor is forced to incur these substantial fees over the next six months.

The FTC argues that Debtor overestimates its costs to defend against the Enforcement Action. The FTC asserts that the declaration of Neal Goldfarb submitted by Debtor in support of its request lacks sufficient detail to support Debtor's proposed estimate. Moreover, the FTC argues that the estimate overstates the amount of estimated trial time and fails to consider that some of the issues in the Enforcement Action will be narrowed, if not eliminated, by summary judgment since the FTC's position is that the uncontested facts establish Debtor's liability.

The FTC further contends that the relevant comparison under FAMCO is not between Debtor's costs of defending itself against the

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[16] In a chapter 11 bankruptcy case, all post-petition obligations have administrative priority status. This means that those claims are paid prior to most other claims in a bankruptcy estate, namely other priority claims and pre-petition unsecured claims. In addition, those claims must be paid in full on the effective date of a confirmed plan of reorganization. The effective date is usually 30 days after an order confirming a plan of reorganization is entered, but can be in as few as eleven days. To stay administratively solvent, a debtor would insure that debtor retains sufficient cash reserves on hand to pay all administrative claims in full on the effective date of a plan.

FTC in the Florida Court or not defending itself at all, but rather between Debtor defending itself in the Florida Court and defending itself in this Court. According to the FTC, unless the Enforcement Action is concluded as to Debtor, the same facts will have to be litigated in this Court to establish a bankruptcy claim against Debtor.[17] Moreover, under the recently enacted changes to the Bankruptcy Code, the FTC can pursue a non-dischargeability action against Debtor for the FTC's monetary claim. Finally, the FTC alleges that it would pursue the non-monetary aspects of the Enforcement Action after confirmation of Debtor's plan. NRG Energy, 457 F.3d at 780-81 (holding that a bankruptcy court has no authority to enjoin a government agency from bringing a post-confirmation enforcement action against a reorganized debtor for injunctive relief against future law violations).[18]

The FTC does not address the second harm raised by Debtor: the impact of the continuation of the Enforcement Action on Debtor's reorganization efforts. Debtor has relatively few employees and Debtor's president, Mr. Dawson -- one of the founders of Debtor -- is and will continue to be very closely involved in Debtor's defense in the Enforcement Action. Mr. Dawson is also the main contact for all of Debtor's reorganization efforts in addition to

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[17] This argument is incorrect, or at least premature, because the Court is only enjoining the Enforcement Action for a few months and has not determined whether the Enforcement Action will be adjudicated in the Florida Court or in this Court, if it ultimately needs to be adjudicated at all. It might well settle in the bankruptcy context in connection with a plan of reorganization or otherwise. In this connection, the desire of the post-petition Debtor and the FTC to resolve their disputes may be significantly greater than the situation before Debtor filed for bankruptcy.

Furthermore, even if the matter were tried in the bankruptcy court, this Court would determine when the trial should take place.

[18] However, as noted, Debtor and the FTC may well settle those disputes in the context of Debtor's plan of reorganization or otherwise.

his duties overseeing normal operational issues. The bankruptcy filing unsettled Debtor's customers and Debtor is working on a proposed pre-payment plan whereby Debtor would pay 50% of the receivables represented by post-petition billing submissions. Because this is a new program, the program will be time-consuming to implement and monitor. In addition, Mr. Dawson needs to be available to work with Debtor's reorganization counsel, the various secured and unsecured creditors, the Committee and the United States Trustee.

Further, the Committee supports Debtor's use of cash collateral through November 2, 2007. In exchange, Debtor has committed to negotiate with the Committee a term sheet for a plan of reorganization contemplating a continuation of Debtor's business operations with the goal of allowing Debtor to exit bankruptcy as quickly as possible. Debtor is also monitoring the possible sale of PaymentOne to a third party.

Finally, upon Debtor filing its chapter 11 bankruptcy petition, Debtor became a "debtor-in-possession." As a debtor-in-possession, Debtor acts as a fiduciary to the bankruptcy estate and owes a duty of care and loyalty to the bankruptcy estate's creditors. In re McConville, 110 F.3d 47, 50 (9th Cir. 1997). Thus, Debtor thus is a new entity with different and additional responsibilities, concerns and pressures than it had when Debtor operated solely as Integretel. Debtor, the Committee and Debtor's other creditors need time to evaluate the merits and strengths of the FTC's positions and decide whether the bankruptcy estate should try to settle the Enforcement Action with the FTC. Giving Debtor and Debtor's creditors a few months to do that is critical at this

juncture -- particularly in the context of negotiating a plan of reorganization.

3. Balancing of the Harms and the Public Interest

Based on the unique facts of this case and in consideration of the relative hardship of the parties and the public interest concerns, the Court finds that continued prosecution of the Enforcement Action severely threatens the integrity of the bankruptcy process and Debtor's prospects for reorganization and a preliminary injunction of the Enforcement Action against Debtor through March 14, 2008 is warranted. On March 7, 2008 at 1:00 p.m., the Court will hold a further hearing on whether the preliminary injunction of the Enforcement Action should be continued beyond March 14, 2008. Either the FTC or Debtor may request that the preliminary injunction be lifted before March 7, 2008 for good cause based on facts that are not currently before this Court.

The FTC is concerned that this Court's granting of a preliminary injunction against the Enforcement Action will set a precedent that a defendant can escape prosecution for committing deceptive and unfair trade practices by simply filing for bankruptcy. The Court is keenly aware of the FTC's concern and that is not what this Court intends. Rather, it is the unusual convergence -- almost a perfect storm -- of the trial schedule in the Enforcement Action and the critical first few months of a viable chapter 11 bankruptcy case that warrant a limited preliminary injunction at this time.

First, the next several months are a critical time for Debtor in its effort to reorganize, and the immediate continuation of the

Enforcement Action seriously threatens Debtor's ability to reorganize. Debtor has only 37 employees to service its 58 pre-petition customers and manage Debtor's relations with over 1400 LECs. Moreover, Debtor's president, Mr. Dawson, is and will continue to be closely involved in Debtor's defense in the Enforcement Action. If the Enforcement Action is not temporarily stayed, Mr. Dawson would be required to divert his time and attention from Debtor's reorganization between November 6 and December 4, 2007 to assist Debtor's counsel in the Enforcement Action in preparing an opposition to a motion for summary judgment that the FTC has stated it will file against Debtor. There may also be eleven or more additional depositions in which Debtor will need to participate if the Florida Court grants the pending motions requesting additional discovery. In addition, Mr. Dawson will be required to fly to Florida during February 2008 to prepare for and participate in the trial in the Enforcement Action scheduled to commence on February 25, 2008.[19] The diversion of Debtor's management -- and Mr. Dawson in particular -- in defending the Enforcement Action during the next few months seriously threatens Debtor's reorganization.

Mr. Dawson is the main contact for all of Debtor's reorganization efforts in addition to his duties overseeing normal operational issues. Debtor's reorganization efforts -- especially at this early stage of Debtor's bankruptcy case -- are time-consuming. First, under the Bankruptcy Code, Debtor is required to

[19] The trial situation could possibly change if FTC does file a summary judgment motion and it is granted in part or in full. However, Debtor will still need to prepare for trial because Debtor cannot know in advance what the result will be of any as yet to be filed FTC motions.

obtain court approval for the use of its cash collateral post-petition. This is a marked difference from how Debtor operated pre-petition. Pre-petition Debtor could use any cash that came into Debtor's accounts subject only to claims of various creditors. Post-petition, however, Debtor must obtain the consent of all creditors who have an interest in that cash collateral or court approval for the use of that cash collateral. In this instance, the Court has approved Debtor's use of cash collateral on an interim basis at three-week intervals. Debtor has scheduled a final hearing for use of cash collateral for November 2, which depending on the status of its negotiations with its creditors, Debtor may or may not change to another interim request for use of cash collateral.

It is not unusual in a chapter 11 bankruptcy case for a debtor to seek multiple interim requests for use of cash collateral while a debtor negotiates with secured and unsecured creditors for final consent to a debtor's use of cash collateral. In the early stages of a bankruptcy case, creditors are getting up to speed regarding a debtor's business operations and the relative likelihood of recoveries for creditors pursuant to various reorganization proposals. During this time, creditors, debtors and the bankruptcy court strike a balance among the parties' interests and grant limited permission for a debtor to use post-petition cash collateral until the parties are comfortable with a debtor's plans to operate and can resolve a debtor's use of cash collateral on a final basis. The early, limited permission to use cash collateral is in part why a chapter 11 bankruptcy case is so time-intensive for a debtor, and indeed all parties in the early stages.

Second, the bankruptcy filing unsettled Debtor's customers and Debtor is actively working on a proposed pre-payment plan whereby Debtor would pay 50% of the receivables represented by post-petition billing submissions. This is a marked change from Debtor's pre-petition operations where Debtor paid its customers approximately 90 days after the billing transactions were submitted to Debtor. Because the pre-payment program is new, Mr. Dawson and Debtor's other employees will have to spend a great deal of time implementing and monitoring the new program.

Further, the Committee was appointed on October 1, 2007 and on October 10, 2007, the Committee had a five hour face-to-face meeting with Debtor. At that meeting the Committee supported Debtor's use of cash collateral through November 2, 2007 and in exchange Debtor has committed to negotiate with the Committee a term sheet for a plan of reorganization contemplating a continuation of Debtor's business operations with the goal of allowing Debtor to exit bankruptcy as quickly as possible. Debtor is also monitoring the possible sale of PaymentOne to a third party. Mr. Dawson is a, and probably the, critical participant in those discussions and negotiations.

Finally, Debtor has complex business operations and over 1,200 creditors on its creditor matrix. Due to the size and complexity of Debtor's business operations, Debtor requires -- and has been granted -- additional time to complete its Schedules and Statement of Financial Affairs. Those documents are currently due on November 15, 2007. The Schedules consist of seven separate schedules that require Debtor to: (a) list in detail all real and personal property, the value of each piece or category of property,

and the security interest held against that property; (b) provide separate lists of Debtor's creditors -- secured creditors, priority unsecured creditors and unsecured creditors that includes an address for each creditor, information regarding when the claim was incurred and consideration for the claim, whether the claim is contingent, unliquidated or disputed, and the amount of the claim; (c) provide a detailed list of all executory contracts and unexpired leases; and (d) provide a list of all entities that are co-debtors with Debtor. The Statement requires Debtor to answer twenty-five questions in detail regarding Debtor's financial affairs. The questions require Debtor to detail, inter alia, all payments or transfers Debtor made in the 90 days immediately preceding the commencement of the case that aggregate more than $5,475 to any creditor, and all payments or transfers Debtor made within one year immediately preceding the commencement of the case to any creditor that is an insider (all of the majority-owned subsidiaries of Debtor are considered to be insiders).

Based on these projected activities, Debtor's management -- and Mr. Dawson in particular -- will spend the next few months dealing with Debtor's customers and creditors, completing Debtor's Schedules and Statement, negotiating with the Committee over the terms for a plan of reorganization and, if successful, most of November and early December will be spent negotiating a draft plan of reorganization and overseeing the preparation of a proposed disclosure statement. Both of these documents will require substantial amounts of time on the part of Mr. Dawson and Debtor's other personnel. The plan of reorganization is Debtor's contract with its creditors as to how Debtor intends to restructure itself

using the Bankruptcy Code. In addition, the proposed disclosure statement is similar to a prospectus and will require, inter alia, a description of Debtor's background, the events that caused Debtor to file its bankruptcy case, what has changed such that Debtor will be able to complete its proposed plan of reorganization, a description of the proposed plan, and financial projections in support of the plan if Debtor proposes to present a plan that permits Debtor to operate as a going concern. Debtor must submit its proposed disclosure statement to this Court for approval. 11 U.S.C. § 1125(b). Such activities will consume a huge portion of the available time of Debtor's management over the next few months.

However, should Debtor be required to proceed to trial in the Enforcement Action at the end of February 2008, Mr. Dawson and other of Debtor's personnel will be required to travel to Florida and spend many days -- if not weeks in the case of Mr. Dawson -- preparing for and participating in the trial in the Enforcement Action. This activity will take place at a critical juncture of Debtor's bankruptcy case where Debtor should instead be seeking confirmation of a plan of reorganization. Debtor is committed to proposing a plan of reorganization on an expeditious basis. Under the notice requirements of the Bankruptcy Code and Rules, it is highly likely that Debtor will seek approval of a disclosure statement during January 2008, and could set a confirmation hearing on a proposed plan of reorganization during February or March 2008.

Confirmation of a chapter 11 plan requires an enormous amount of work for both a debtor and its counsel. In addition to resolving and addressing any objections by any parties to approval of a disclosure statement and confirmation of a plan, this Court

has an independent duty to ensure that a disclosure statement contains adequate information, In re Main Street AC, Inc., 234 B.R. 771, 774 (Bankr. N.D. Cal. 1999), and an affirmative duty to ensure that a plan satisfies all sixteen requirements of Bankruptcy Code section 1129 for confirmation. In re Ambanc La Mesa Ltd. P'ship., 115 F.3d 650, 653 (9th Cir. 1997). Just one of the requirements is that this Court must determine that confirmation of Debtor's plan will not likely be followed by the liquidation or further financial reorganization. 11. U.S.C. § 1129(a)(11). Mr. Dawson will almost certainly be required to testify before this Court as to Debtor's plan and the financial projections on which it is based, as well as other evidence this Court requires to confirm any proposed plan submitted for confirmation by Debtor.

In addition to the impact of the Enfrocement Action on Debtor's president and other personnel, it would be highly injurious to Debtor and Debtor's prospects for reorganization if Debtor had to spend the bulk of the estimated $1 million in legal fees and costs associated with the Enforcement Action during this same critical period. Such an outlay of funds at a critical time of confirmation would seriously impair, if not strike a death knell, to Debtor's prospects for a reorganization. Debtor is required under the Bankruptcy Code to pay all administrative claims as of the effective date of a confirmed plan. 11 U.S.C. § 1129(a)(9)(A). Debtor may well not have sufficient funds to both pay the litigation costs of defending the Enforcement Action and pay administrative claims on the effective date of a confirmed plan.

The FTC likely holds only a pre-petition unsecured claim against Debtor in the Enforcement Action. Any monetary claims FTC asserts against Debtor arise only from Debtor's alleged pre-petition placing of unauthorized collect call charges onto consumers' telephone bills. There is no showing that at this point there is any reason for Debtor to spend $1 million litigating an unsecured claim in the next five months. First, at this juncture it is unclear what unsecured creditors will receive in Debtor's reorganization and it is unknown if spending $1 million to defend against the FTC's claims makes sense, especially in this case where secured and other unsecured creditors desperately need for all resources to be devoted to Debtor's reorganization efforts. Second, over the next five months Debtor may negotiate a resolution of the FTC's claims without the need for litigation. This Court is not determining at this juncture where the FTC's claims will be liquidated. Rather, this Court is merely delaying briefly the Enforcement Action against Debtor only.[20] It is this Court's experience that in chapter 11 cases such as Debtor's, a debtor typically negotiates with the various creditors to reach a consensus as to the structure of a plan of reorganization. It is generally less expensive and easier if a debtor can negotiate a plan of reorganization than if a debtor has to confirm a plan of reorganization over the objections of numerous creditors. At the early stages of Debtor's case and under the facts of this case, a preliminary injunction of limited duration is warranted.

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[20]This Court's decision stays the Enforcement Action against Debtor for a few months. This decision does not determine whether (1) the FTC may recommence the Enforcement Action in the Florida Court after those few months, or (2) whether the FTC should be required to pursue Debtor by filing a claim with, and litigating that claim in, the bankruptcy court.

By limiting the duration of the preliminary injunction and requiring Debtor to provide further updated evidence in mid-February 2008 to support the continued injunction of the Enforcement Action, this Court eliminates or at least reduces substantially the alleged harms of the FTC. The FTC cites three harms from a possible injunction of the Enforcement Action: (1) the inability of the FTC to obtain the non-monetary equitable relief it seeks against Debtor; (2) the inability of the FTC to pursue the claims in the Enforcement Action against Debtor in the Florida Court; and (3) the public interest in permitting the FTC to pursue a vital enforcement strategy to curb the unlawful practice of placing unauthorized charges on consumers' phone bills. However, this Court has not eliminated, and is not eliminating, the possibility that at a later date this Court would permit the FTC to prosecute the Enforcement Action in the Florida Court, including the ability of the FTC to obtain the non-monetary equitable relief it seeks against Debtor. The FTC itself notes that it will seek such relief against Debtor post-confirmation. This Court is merely delaying for a few months the FTC's prosecution of the Enforcement Action against Debtor. No decision has yet been made as to where the FTC's claims will be litigated if indeed those claims need to be litigated at all.

Granting a preliminary injunction of limited duration also renders premature the FTC's argument that this Court must consider Debtor's costs of Debtor defending itself in the Florida Court and defending itself in this Court rather than Debtor's costs of defending itself against the FTC in the Florida Court or not defending itself at all. First, Debtor will not likely be

prosecuting an objection to the FTC's claim in the next few months. Indeed, March 14, 2008 is the claims bar date for governmental units in Debtor's bankruptcy case. Thus, for this limited duration preliminary injunction, Debtor almost certainly will not incur any costs defending itself in this Court against the FTC's claims.[21]

C. Contempt Proceedings and Turnover Action

1. Debtor's Ability to Sue the Receiver

Receiver argues that this Court lacks subject matter jurisdiction over this adversary proceeding as to Receiver because Debtor has not obtained permission from the Florida Court to bring this action -- or any action -- against Receiver. Receiver asserts that for over 100 years, legal authority holds that a litigant must obtain permission from the court appointing a receiver before bringing an action against that receiver. Carter v. Rodgers, 220 F.3d 1249, 1252 (11th Cir. 2000) (holding that under Barton v. Barbour, 104 U.S. 126 (1881), a debtor must obtain leave from the bankruptcy court before the debtor can initiate an action in district court against a bankruptcy-court appointed trustee for breach of fiduciary duties); In re Crown Vantage, Inc., 421 F.3d 963, 970 (9th Cir. 2005) (a bankruptcy-court appointed trustee of a liquidating trust cannot be sued in a foreign jurisdiction for violating a settlement agreement without the permission of the court appointing the trustee).

Debtor asserts that the Barton doctrine applies only if Debtor were suing Receiver for dereliction of duties, which Debtor is not doing in this adversary proceeding. Moreover, Debtor argues that Crown Vantage stands for the proposition that Debtor does not need

[21] See footnote 17, supra.

leave from the Florida Court to sue Receiver in this instance because this Court has exclusive in rem jurisdiction to determine the property of Debtor's bankruptcy estate and the injunctive relief requested by Debtor is a stay specifically designed to protect the assets of the bankruptcy estate, so the Barton doctrine is not invoked.

This Court agrees with Debtor that once Debtor filed its bankruptcy petition on September 16, 2007, this Court obtained exclusive in rem jurisdiction over the property in Debtor's bankruptcy estate, and particularly over any legal and equitable interest Debtor held in the Commingled Funds as of the commencement of the case. While none of the parties or this Court have found any cases directly on point, the Court finds Gilchrist v. General Elec. Capital Corp., 262 F.3d 295 (4th Cir. 2001) particularly instructive.

In Gilchrist, Spartan International, Incorporated and its subsidiaries (collectively, "Spartan") closed their doors for business. Spartan's major creditor ("GE") commenced a state law debt-collection action invoking the diversity jurisdiction of the district court of South Carolina ("South Carolina Court"). To facilitate the foreclosure of the creditor's lien, the South Carolina Court appointed a federal receiver for all of Spartan's assets ("Receiver Order"). The Receiver Order enjoined all persons from commencing or prosecuting any action, suit or proceeding that affected the receivership estate or Spartan. Gilchrist, 262 F.3d at 297-98.

One week later and with actual notice of the Receiver Order, 50 creditors ("Georgia Creditors") filed an involuntary bankruptcy

petition in the bankruptcy court in the Southern District of Georgia ("Georgia Court") and a request for the appointment of an interim bankruptcy trustee. GE objected to the appointment of an interim bankruptcy trustee and filed a motion to dismiss the involuntary bankruptcy petition or transfer venue to the district of South Carolina. The receiver filed a similar motion. Following a hearing, the Georgia Court overruled the objections, denied the motions and appointed an interim bankruptcy trustee. Gilchrist, 262 F.3d at 298.

While that hearing was in progress, the receiver obtained a temporary restraining order from the South Carolina Court enjoining 38 of the Georgia Creditors from undertaking any action in furtherance of the involuntary bankruptcy petition. Four days later the South Carolina Court found the Georgia Creditors in contempt of the Receiver Order and allowed the Georgia Creditors to purge their contempt by withdrawing the bankruptcy petition. The interim bankruptcy trustee argued that the automatic stay precluded the South Carolina Court's actions, but the South Carolina Court refused to recognize the automatic stay of its proceedings. The South Carolina Court asserted that it had jurisdiction to determine the scope of the automatic stay, and it had the authority to issue an injunction to prevent the collateral attack of that court's Receiver Order appointing the receiver. In an effort to purge their contempt, the Georgia Creditors subsequently filed a petition in the Georgia Court to withdraw the involuntary petition, which the Georgia Court denied. The Georgia Court stayed further proceedings pending a review of the South Carolina Court's orders by the Fourth Circuit. Gilchrist, 262 F.3d at 298-99.

In reviewing the South Carolina Court's orders, the Fourth Circuit noted that the South Carolina Court was within the scope of that court's equitable powers in appointing the receiver and asserting in rem jurisdiction over Spartan's assets, even those located in other districts. Gilchrist, 262 F.3d at 302. However, once the Georgia Creditors filed the involuntary bankruptcy petition,

> [b]y virtue of the jurisdictional provisions of the United States Code, and the commencement of a bankruptcy case against Spartan, the bankruptcy court obtained "*exclusive* jurisdiction of all of the property, wherever located, of [Spartan] as of the commencement of such case, and of property of the estate." 28 U.S.C. § 1334(e) (emphasis added). In addition, the filing of the petition in bankruptcy "operates as a stay, applicable to all entities, of the ... continuation ... of a judicial, administrative, or other action or proceeding against the debtor that was commenced before" the bankruptcy petition. 11 U.S.C. § 362(a)(1). To give effect to its jurisdiction, the bankruptcy court is given broad equitable powers, *see* 11 U.S.C. § 105, with nationwide service of process, *see* Bankr. R. 7004(d).

Gilchrist, 262 F.3d at 303.

The Fourth Circuit then found that the South Carolina Court had properly determined that the South Carolina Court had jurisdiction to determine its own jurisdiction and the scope of the automatic stay. However, the Fourth Circuit stated that:

> The [South Carolina] court provided no explanation of why, as a matter of equity, the bankruptcy process was not superior to a receivership in the liquidation of a large business, with assets in several jurisdictions and with thousands of creditors, some of whom were claiming liens superior to the lien relied upon by GE when it initiated the receivership proceeding. More importantly, it provided no explanation of why the terms of § 362(a) were not applicable.
>
> Similarly, in their briefs and arguments presented to us, counsel for GE and the receiver advanced no exception to § 362(a) that would be applicable. Instead, they argued for a "first-filed" principle, urging that the court which first takes custody of assets for liquidation should be given priority.

We cannot agree. Our examination of the Bankruptcy Code reveals that Congress intended that the bankruptcy process be favored in circumstances such as these. Section 1334(e) of title 28 is unequivocal in its grant of exclusive jurisdiction to the bankruptcy court, and § 362(a) imposes an automatic stay on all proceedings merely upon the filing of a bankruptcy petition. If we were to frustrate these express provisions to further a first-filed policy, we would have to deny bankruptcy jurisdiction to every bankruptcy court in which foreclosure proceedings had already commenced against the debtor's property, on the grounds that the *in rem* nature of the foreclosure proceeding precludes the bankruptcy court from taking custody of the *res*. Such a jurisdictional limitation on bankruptcy proceedings would severely limit the efficacy of bankruptcy. In the absence of express language suggesting that Congress intended for bankruptcy jurisdiction to be so limited, we believe it would frustrate Congressional intent to imply such a limitation based solely on consideration of a first-filed policy.

Even if general equitable principles could modify the application of statutory jurisdictional grants, we do not believe that the equities favor the common-law receivership process over the highly developed and specific bankruptcy process. The procedural requirements for liquidating a large corporation with thousands of creditors, many of whom might challenge the priority of liens and the adequacy of asset sales, present a task that would push the receivership process to its limits. *See* [In re Baldwin-United Corp. Litigation], 765 F.2d [343, 348 (2nd Cir. 1985)] ("[T]o whatever extent a conflict may arise between the authority of the Bankruptcy Court to administer this complex reorganization and the authority of the District Court to administer consolidated pretrial proceedings, the equities favor maintenance of the unfettered authority of the Bankruptcy Court"). In this case it can be seen, even from the initial transactions in the receivership, that the customized receivership mechanisms are wanting in comparison with established bankruptcy process. For example, when the receiver in this case sold a mill in Georgia for $4.2 million, the creditors had no advance notice of the transaction, and some have challenged the adequacy of compensation, proffering evidence that the mill was worth over $20 million. More important to the Georgia creditors in this case, the district court did not have in place a mechanism to adjudicate the relative priority of liens. GE claims a first lien by reason of its perfected security interest in most of the assets of Spartan and proffered an order by which the proceeds of liquidation would be paid to it as the superior lien holder. But Spartan's employees claim a prior statutory lien in assets produced by them at the manufacturing plants at which they worked, as created by state law.

> While they surely could file claims in the receivership, the process for making and adjudicating such claims was not spelled out.

Gilchrist, 262 F.3d at 303-04.

While the facts in this case differ from those in Gilchrist -- the action in the Florida Court is an enforcement action rather than an action to foreclose on collateral, and Debtor is not the receivership entity as in Gilchrist, there are two primary principles that apply here. First, as noted in Gilchrist, once a bankruptcy petition is filed, section 1334(e) of title 28 is unequivocal in its grant of exclusive jurisdiction to the bankruptcy court over all property, wherever located, of Debtor as of the commencement of such case. 28 U.S.C. § 1334(e). Property of the bankruptcy estate includes all legal or equitable interests of a debtor in property as of the commencement of the case. 11 U.S.C. § 541(a)(1). Bankruptcy Code section 542 also provides that entities -- other than custodians -- in possession, custody or control of property that a debtor-in-possession may use, sell, or lease under Bankruptcy Code section 363 shall deliver and account for such property to that debtor, unless the property is of inconsequential value or benefit to the estate. 11 U.S.C. § 542(a). Bankruptcy Code section 543 provides that a custodian shall turn over property of the debtor unless excused by the bankruptcy court. 11 U.S.C. §§ 543(b), (d).

Here Receiver asserts that because the Florida Court found in the Omnibus Order that Integretel held "reserves" in the amount of $1,762,762.56 on behalf of the Prior Customers as of June 30, 2007, Integretel was required to turn over the Commingled Funds to Receiver. However, the Commingled Funds were nothing more than

Integretel's commingled funds and were not any particular or identifiable *res*, and the Florida Court did not find that a *res* existed. In fact the Omnibus Order does not require Integretel to pay any specific amount of funds to Receiver. Rather, in order to comply with the Omnibus Order, Debtor would have to pay Receiver out of Debtor's general account the "reserves" the Florida Court determined Integretel held on behalf of the Prior Customers (the Florida Court described such "reserves" but did not quantify them). Integretel did not turn over any commingled funds to Receiver pre-petition and Debtor did not segregate any such funds in any fashion pre-petition. As of the petition date, Debtor retained an interest in all of its commingled funds and Receiver asserted an interest in some as yet unquantified portion of those funds. On the petition date, this Court obtained exclusive jurisdiction over all of the commingled funds under section 1334(e) of title 28. Accord In re Simon, 153 F.3d 991, 996 (9th Cir. 1998).[22]

It is this exclusive grant of in rem jurisdiction that precludes the application of the Barton doctrine in this particular set of circumstances. Crown Vantage points out that

> [p]art of the rationale underlying Barton is that the court appointing the receiver has in rem subject matter jurisdiction over the receivership property. As the Supreme Court explained, allowing the unauthorized suit to proceed "would have been a usurpation of the powers and duties which belonged exclusively to another court." (Citations and footnote omitted).

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[22] Because there is no pre-petition *res*, it is difficult to understand how the Commingled Funds could not be property of the bankruptcy estate. This Court is not reviewing the Florida Court's decision in the Omnibus Order; that decision is on appeal to the Eleventh Circuit. However, this Court is of the opinion that the bankruptcy court has exclusive jurisdiction over what constitutes property of the estate. See Section III.C.2 of this decision, infra. In any event, the Court must consider Debtor's likelihood of success on the merits on this issue in considering the stay issues currently before the Court.

Crown Vantage, 421 F.3d at 971. It is the unique situation here -- where the exclusive in rem jurisdiction over the Commingled Funds passed from the Florida Court to this Court upon Debtor filing its bankruptcy petition -- that eliminates Debtor's need to request leave from the Florida Court before suing Receiver in this adversary proceeding.

The parties dispute the precise implication of the Omnibus Order. Receiver and the FTC assert that the Omnibus Order determined in a final appealable order that the Commingled Funds were property of the receivership estate and Debtor had no interest in the Commingled Funds at the time Debtor commenced this bankruptcy case. Receiver bases this argument on the premise that the Florida Court ordered the turnover of Commingled Funds.

Outside of bankruptcy, Receiver could perhaps compel adherence to the Omnibus Order regardless of whether any actual, segregated funds existed from which to make the payment ordered by the Florida Court. However, once Debtor filed for bankruptcy protection, the Omnibus Order command could only be enforced at the expense of all other creditors of Debtor -- secured and unsecured -- other than Receiver. This distinction is usually discussed in the context of a constructive trust remedy, where courts have often expressed that the "privileging of one unsecured claim over another clearly thwarts the principle of ratable distribution underlying the Bankruptcy Code." In re Flanagan, -- F.3d --, 2007 WL 2915812, *8 (2d Cir. Oct. 9, 2007).

The Ninth Circuit has recognized this distinction for more than 40 years. In Elliot v. Bumb, 356 F.2d 749, 754-55 (9th Cir. 1966), the Ninth Circuit refused to allow state law to control

whether a creditor would be entitled to claim that a trust existed over a debtor's commingled funds because the state law yielded to bankruptcy law and bankruptcy law requires tracing. The Ninth Circuit has followed that case in Matter of Esgro, Inc., 645 F.2d 794, 798 (9th Cir. 1981); In re North American Coin & Currency, Ltd., 767 F.2d 1573, 1575 (9th Cir. 1985); and In re Advent Management Corp., 178 B.R. 480, 488 (9th Cir. BAP 1995), aff'd, 104 F.3d 293 (9th Cir. 1997). As noted in Flanagan, the "equities in bankruptcy are not the equities of the common law." Flanagan, 2007 WL 2915812 at *8 (quoting XL/Datacomp, Inc. v. Wilson (In re Omegas Group, Inc.), 16 F.3d 1443, 1452 (9th Cir. 1994)).

Thus, the Omnibus Order is likely, at most, nothing more than a money judgment determining Debtor's purported liability to the receiver.[23] While it is based on the concept that Receiver had a property interest in Debtor's bank accounts as of the issuance of the TRO, the Omnibus Order does not and could not call for the turnover of any specific, identifiable property in Debtor's bank accounts as of the TRO. Rather the Omnibus Order merely directs Debtor to pay over the amount of Debtor's "reserve" liability from any funds Debtor has available to it. Receiver never claimed that Receiver can trace the funds received by Debtor from the Prior Customers to an identifiable fund that still exists. Rather, Receiver correctly interprets the payment order as being a judgment commanding the payment of an as yet unquantified amount of money.

Debtor filed its bankruptcy petition while the Commingled Funds remained in Debtor's bank account. Debtor has demonstrated a

[23] It is not 100 percent clear that the Florida Court has determined that Receiver has a fully liquidated final appealable judgment for money against Debtor.

very strong likelihood of success on the merits -- that whether measured at the outset of the Florida Action or as of the date of the petition, Debtor holds no specific identifiable funds that can be traced from the Prior Customers to Debtor's existing bank accounts. The determination that Receiver held an interest in the Commingled Funds did not eliminate any interest Debtor's bankruptcy estate had in the same funds.

> To reclaim money or property from a bankruptcy estate on the basis that the property belongs to the reclaiming party and not to the debtor, the reclaiming party must be able to definitively trace its property. Even when property is commingled, that property must be positively identified, or else the reclaiming party is relegated to the status of a general unsecured creditor, regardless of the equities. The manner in which the debtor or the estate came into possession of the property is irrelevant. (Citations omitted.)

In re Graphics Technology, Inc., 306 B.R. 630, 635 (8th Cir. BAP), aff'd, 113 Fed. Appx. 734 (8th Cir. 2004). Thus, notwithstanding any post-petition pronouncement by the Florida Court to the contrary, the Commingled Funds are property of Debtor's bankruptcy estate subject to whatever interest the Omnibus Order granted Receiver in those funds -- along with the interests Debtor's other secured and unsecured creditors assert in those funds. Debtor can sue Receiver without obtaining the permission of the Florida Court here because any action by Receiver in furtherance of obtaining possession of the Commingled Funds interferes with this Court's exclusive in rem jurisdiction over those funds.

The second primary principle found in Gilchrist is that a district court is limited in its ability to address competing claims over the same assets. As noted in Gilchrist, even where the receiver held property of Spartan pursuant to the foreclosure

action initiated by GE, the South Carolina Court did not have in place a mechanism to adjudicate the relative priority of liens against that property. In this case, the Florida Court had jurisdiction only over part of Debtor's property pre-petition -- i.e., some portion of the commingled funds in Integretel's bank account. At the time that the Florida Court entered the Omnibus Order, the only parties before that court with respect to the Commingled Funds were Receiver, Integretel and possibly the FTC. The Florida Court could not and did not adjudicate the competing claims to the Commingled Funds asserted by Debtor's secured and unsecured creditors.

2. Bankruptcy Court Jurisdiction Over Property of the Estate

Receiver and the FTC assert that the Florida Court determined that the Commingled Funds were not property of Debtor in the post-petition Clarification Order.[24] In particular, the Florida Court stated with respect to its determination that there was no automatic stay in place as to the contempt proceedings that:

> First, the automatic stay applies only to protect property of the bankruptcy estate or property of the debtor. See 11 U.S.C. § 362(a)(2). The Court has already ruled that the reserve funds are neither the property of the "bankruptcy estate" nor Integretel.

Clarification Order at 4. The issue of the Florida Court's jurisdiction to determine the scope of the automatic stay is not before this Court. However, as discussed above, once Debtor filed its bankruptcy petition, the bankruptcy court has exclusive

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[24] The Clarification Order was issued post-petition. If this Court is correct, that the Florida Court had no jurisdiction to determine post-petition what property constitutes property of the estate, then the Florida Court lacked jurisdiction to issue that aspect of the Clarification Order. The Court considers this matter in the context of the stay issues before it, and not in review of the Florida Court.

jurisdiction to determine what is property of the estate. Gilchrist, 262 F.3d at 303 (once a bankruptcy petition is filed, section 1334(e) of title 28 is unequivocal in its grant of exclusive jurisdiction to the bankruptcy court over all property, wherever located, of a debtor as of the commencement of such case). Moreover, the pre-petition determination that Receiver held an interest in the Commingled Funds did not eliminate any interest Debtor's bankruptcy estate had in the same funds, especially since those funds were not part of a specific pre-petition *res*.[25] See Graphics Technology, 306 B.R. at 635. Thus, the post-petition assertion by the Florida Court in the Clarification Order that the Commingled Funds are not property of Debtor's bankruptcy estate exceeded the Florida Court's post-petition jurisdiction over property of Debtor's estate.[26]

3. Harms to Receiver

Receiver asserts that several harms would occur should this Court enjoin Receiver from implementing or enforcing the Omnibus Order and/or unblock the funds held in the Blocked Account. Primarily, Receiver argues that Debtor is attempting to interfere with the administration of the receivership in seeking to enjoin the enforcement of the Omnibus Order. The purpose of the receivership is to marshal and preserve the assets of the receivership entities in order to return those assets to the

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[25] The creation of the Blocked Account post-petition also does not create a pre-petition *res* since Debtor and Receiver agreed that the temporary establishment of the Blocked Account did not in any way affect the merits of either parties' rights, claims or defenses with respect to the funds in the Blocked Account.

[26] The Clarification Order is currently on appeal to the Eleventh Circuit, but that does not change this Court's legal analysis of the jurisdiction of the bankruptcy court. See footnote 24, supra.

victims of the fraud. Eller Industries, Inc. v. Indian Motorcycle Manufacturing, Inc., 929 F. Supp. 369 (D. Colo. 1995); Citibank, N.A. v. Nyland (CF8) Ltd., 839 F.2d 93 (2d Cir. 1987).[27] In some federal governmental enforcement actions, a federal district court may appoint a receiver and issue a temporary restraining order and/or preliminary injunction to preserve the assets that result from the actions of the receivership entities -- whether held by parties or non-parties -- to provide redress for the legitimately-defrauded investor. FTC v. Productive Marketing, Inc., 136 F.

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[27] Receiver asserts that Eller Industries (a Colorado district court decision which is distinguishable and not binding on this Court in any event) involves a strikingly similar set of facts. According to Receiver, the Colorado district court concluded that the Massachusetts bankruptcy court's injunction could not be effective against a receiver appointed by the Colorado district court because the bankruptcy court's injunction interfered with the Colorado district court's mandated obligations of the receiver -- who was a fiduciary of the Colorado district court and was responsible for locating and protecting the assets of the receivership estate. The Colorado district court found that the purposes of the receivership can only be achieved by a stay of foreign equitable actions, including the Massachusetts adversary proceeding.

This Court disagrees. The facts of Eller Industries are distinguishable and the legal proposition for which Eller Industries stands is not applicable to the instant case. In Eller Industries, a chapter 7 trustee obtained a temporary restraining order against Indian Motorcycle Manufacturing, Inc. ("IMMI") precluding IMMI from soliciting funds by using a script "Indian" trademark. The temporary restraining order enjoined IMMI from transferring, assigning, conveying, hypothecating or encumbering -- except in the ordinary course of business -- any and all of IMMI's assets. Shortly thereafter, a federal receivership was established putting a receiver in as the only officer and director of IMMI. After the federal receiver was appointed, the Massachusetts bankruptcy court converted the temporary restraining order into a preliminary injunction and the bankruptcy trustee asserted that the preliminary injunction applied to the receiver. The Colorado district court held that the Colorado district court had exclusive jurisdiction over the assets and administration of the receivership imposed on IMMI , only the Colorado district court could authorize equitable actions against the receivership estate, and the bankruptcy court's preliminary injunction was not effective against the Colorado district court or the IMMI federal receivership.

In Eller Industries a bankruptcy trustee was enjoining a third party entity that itself was under federal receivership. Such a pursuit was precluded by the federal receivership district court. Here, this Court is enjoining Receiver from dissipating property of Debtor's bankruptcy estate. Debtor is not in receivership. As discussed in detail supra, once Debtor filed its bankruptcy petition, this Court obtained exclusive in rem jurisdiction over the Commingled Funds. No such transfer from the bankruptcy estate to the IMMI federal receiver occurred in Eller Industries, and that case is distinguishable.

Supp. 2d 1096, 1104-06 (C.D. Cal. 2001) (where the district court found that the non-party's failure to turn over receivership funds disrupted the district court's power to enforce its injunction and the receiver's right to obtain such funds). The Florida Action is an enforcement action in which the FTC seeks injunctive relief against Debtor -- among others -- for consumer redress for deceptive and unfair practices for unauthorized billing of charges on phone bills in violation of the Federal Trade Commission Act. The Florida Court appointed Receiver, issued the Preliminary Injunction and ordered Receiver, as the Florida Court's agent, to locate, marshal and preserve receivership property. Receiver argues that if this Court enjoins Receiver from performing Receiver's duties, this Court will also be enjoining the Florida Court. Receiver asserts that such a ruling would create an unworkable, unthinkable, and grave conflict between this Court's injunction order and the previously-issued orders of the Florida Court. However, that is not correct. Bankruptcy courts enjoin parties from proceeding outside of the bankruptcy court; they do not normally enjoin any other courts from taking any action. This Court is not enjoining the Florida Court.

Receiver also argues that Debtor is merely seeking to re-litigate the parties' disputes over the Commingled Funds as set forth in the Omnibus and Clarification Orders. Such re-litigation is barred by res judicata. According to Receiver, a review of the Omnibus Order and the Clarification Order reveals that those orders were not merely an interim measure to preserve the Commingled Funds. Rather those orders adjudicated ownership of the Commingled Funds. Moreover, the ownership issue is not predicated on whether

the FTC ultimately prevails in the Enforcement Action, and the turnover provisions of the Omnibus Order and Clarification Order are final, appealable orders. The FTC contends that any issue that Debtor has with those orders should be brought before the Eleventh Circuit. However, the bankruptcy court has exclusive in rem jurisdiction post-petition over property of the estate, as well as jurisdiction to determine what constitutes property of the estate, so Debtor necessarily should be permitted to assert that position in this Court.

Additionally, Receiver is concerned about the dissipation of the Commingled Funds should the Blocked Account be unblocked. If Debtor were to spend the funds in the Blocked Account, the purpose of the Omnibus Order will be thwarted. Also, if this Court were to enjoin Receiver and permit Debtor to use the Commingled Funds in the operation of its business, this Court would be exercising control over property under which the Florida Court has exclusive in rem jurisdiction and this Court would effectively be determining the interests in the Commingled Funds without a final order in an adversary proceeding in contravention of Federal Rule of Bankruptcy Procedure 7001(2).

Debtor contends that Receiver is adequately protected, even assuming Receiver has a specific interest in the Commingled Funds. Because this Court is not unblocking the Blocked Account at this time, there is no need to address Debtor's argument that Receiver is adequately protected by Debtor's total assets even if at a later time Receiver were to demonstrate an interest in the Commingled Funds and the Court were to consider whether to unblock all or some of the funds in the Blocked Account.

4. Harms to Debtor

Debtor asserts that it will face irreparable injury if enforcement of the Omnibus Order is not enjoined[28] and if the Blocked Account is not unblocked. First, Debtor's business will suffer very substantially and irreparably if Debtor is required to turn over $1,762,762.56 to Receiver under the Omnibus Order, particularly at this critical point in Debtor's reorganization efforts. Debtor's estate will lose the over $1.7 million that appears to be property of the estate. Those funds will not be available to Debtor or its creditors if they are turned over to Receiver.

Second, Debtor asserts that it needs those funds to maintain adequate cash reserves relating to its post-petition operations. This in part is due to a shift in Debtor's actions with respect to "unremitted" funds. Specifically, under Debtor's pre-petition settlement process, when Debtor received payments from the LECs, Debtor would settle Debtor's obligations with its customers. Debtor had the right to retain some portion of those proceeds under the service contracts and pay the unremitted portion to the customer at a later time. When Debtor withheld funds during the pre-petition settlement process, Debtor used those funds for its general operating expenses. Post-petition, Debtor believes it is prudent for Debtor to retain sufficient cash to cover Debtor's possible administrative obligations to its customers to remit withheld funds to those customers, should Debtor have to remit those funds in the future. Under its new post-petition policy to retain sufficient cash to cover the unremitted funds, Debtor

[28] Debtor asserted this argument prior to obtaining the Stay Order.

requires additional excess cash to ensure the unremitted funds are available to customers for billing transactions submitted post-petition.

Receiver and the FTC both argue that based on Debtor's own budgets, Debtor does not currently need the use of the funds in the Blocked Account, at this time, so there is no basis for this Court to release those funds. Receiver and the FTC argue that Debtor has made no attempt to supply any foundation for the financial figures. Also, the budgets indicate that Debtor is never left without cash. The total cash balance even during the monthly shortfalls never falls below $3 million. The question then arises as to whether the claimed monthly shortfall in mid-December results from the unsubstantiated legal costs related to the Enforcement Action, the unexplained one-time drop in revenue in December, and/or the unusual and questionable post-petition pre-payment arrangement.

In addition, as Debtor points out, such a turnover by Debtor to Receiver of the funds in the Blocked Account would be a preference of one unsecured creditor -- Receiver -- over all similarly situated unsecured creditors. The portion of the Omnibus Order that requires Debtor to pay over the Commingled Funds likely represents, at most, an ordinary judgment against Debtor which is an unsecured claim in this bankruptcy estate. From the issuance of the TRO and Preliminary Injunction in the Florida Court to the filing of Debtor's bankruptcy case, no money was set aside for Receiver's claim. The Omnibus Order requiring Debtor to pay over to Receiver an amount denominated on Debtor's books as "reserves" cannot create a property interest where none exists. Debtor has "reserve" amounts for each of Debtor's past and current customers,

and none of those customers are being afforded the right to invade Debtor's bank account to retrieve funds that those customers might wish to claim as their own. Receiver's claim is not superior to that of any other creditor, except that Receiver has obtained the Omnibus Order from the Florida Court, which is currently on appeal to the Eleventh Circuit.

In an effort to counter this alleged harm of Debtor, the FTC argues that the Florida Court ruled in the Omnibus Order that the Commingled Funds are property of the receivership estate and not property of Integretel. Moreover, Debtor's purported inability to turn over the funds is a complete defense to contempt under FTC v. Affordable Media, LLC, 179 F.3d 1228, 1239 (9th Cir. 1999), if that defense can be established. FTC argues that if Debtor prevails on the inability to pay defense, Debtor will not have to turn over the Commingled Funds and Debtor will not have the irreparable harm Debtor alleges. Alternatively, if Receiver ultimately prevails, then there is also no cognizable irreparable harm because the property of the receivership estate will have been rightly restored to the receivership at no cost to Debtor's estate.

The FTC further argues that Debtor's claim for irreparable harm rings especially hollow given that Debtor only has itself to blame for any predicament in which Debtor now finds itself. Debtor was served with the TRO in March 2006 and had 18 months to organize its financial affairs in order to comply with the TRO. Debtor had ample opportunity to seek clarification of the Florida Court TRO and Preliminary Injunction, secure a letter of credit, borrow from one of Debtor's affiliated companies, cut costs, or put money into savings. Instead, Debtor allegedly chose to ignore the TRO and

Preliminary Injunction, and Debtor should not now be heard to complain about a harm that is in essence, self-inflicted.

Finally, Debtor will be harmed by incurring legal fees and costs if enforcement of the Omnibus Order is not enjoined, as well as the diversion of Debtor's management from the reorganization process. Debtor estimates that Debtor will incur an additional $50,000 to $150,000 in fees related to Receiver's request for the turnover of the Commingled Funds. Receiver argues that the contempt proceedings are largely complete and the orders are self-executing. However, the Omnibus Order is now on appeal. If the enforcement of the Omnibus Order is not enjoined, Debtor will have to comply with the order to turn over the funds or show cause why Debtor should not be held in contempt.

5. Balancing of the Harms and the Public Interest

Even if the contempt proceeding is properly subject to the exemption from the automatic stay under Bankruptcy Code section 362(b)(4), this Court may enjoin the prosecution of the contempt proceeding under Section 105 if the contempt proceeding "threatens" the assets of the bankruptcy estate. FAMCO, 264 B.R. at 653. A proceeding "that seeks actual physical control over the assets of the debtor's estate threatens the bankruptcy court's exclusive jurisdiction over the *res* of the debtor's estate and therefore can be enjoined." FAMCO, 264 B.R. at 655.[29]

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[29] This Court is not reviewing the Florida Court's decision in the Clarification Order that the contempt proceeding is exempt from the automatic stay under Bankruptcy Code section 362(b)(4); that is on appeal to the Eleventh Circuit. The Florida Court determined that the contempt proceeding was an exercise of the government's police or regulatory power, and therefore exempt from the automatic stay pursuant to Bankruptcy Code section 362(b)(4). However, as this Court understands the situation, neither the FTC nor any other government agency is a party to Receiver's contempt

(continued...)

a. Enjoining Enforcement of the Omnibus Order

Once Debtor filed its bankruptcy petition a bankruptcy estate came into being. Debtor is a debtor-in-possession and is a fiduciary to all of Debtor's creditors -- inter alia, secured creditors, unsecured creditors, customers, the FTC and Receiver. Receiver certainly does not represent all creditors of Debtor's estate. At most Receiver represents the receivership estates of the Prior Customers and the FTC. Receiver does not seek to have the Commingled Funds turned over to him to protect those funds for all creditors of Debtor's bankruptcy estate. Rather, Receiver seeks possession of those funds for the benefit of the receivership estates of the Prior Customers, to the exclusion of Debtor's other secured and unsecured creditors.

Although the Florida Court issued the Omnibus Order, Receiver -- in the shoes of the Prior Customers -- is no different from nearly all of Debtor's customers. The typical service contract provides for Debtor to maintain certain reserves for disputes, fees and other adjustments. These "reserves" on behalf of the Prior Customers were the "reserves" that were the subject of the Omnibus Order. It is undisputed that the "reserves" were held as bookkeeping entries and not as segregated funds. Permitting Receiver to implement the Omnibus Order would irreparably harm Debtor's bankruptcy estate by preferring one creditor -- Receiver -- over other similarly situated creditors of Debtor, since most if not all service contracts provide for the same "reserves."

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[29](...continued)
proceeding.

Moreover, Debtor asserts that it needs the Commingled Funds to operate post-petition. This Court should not destroy Debtor's business to "protect" a creditor that is likely an unsecured creditor, and in the same position as Debtor's other customer creditors.

As far as this Court knows, enforcement of the Omnibus Order is presently stayed under the Stay Order. This is so because on September 20, 2007, the Florida Court issued an order staying proceedings against Debtor. The Clarification Order vacated the September 20, 2007 order. The Stay Order stays the Clarification Order, so the end result is that the Stay Order reinstated the September 20, 2007 order that stays, inter alia, enforcement of the Omnibus Order. At this point, this Court is not inclined to issue a stay that is duplicative of the stay of the Eleventh Circuit. Should there currently be no such stay or should the status of a stay of the enforcement of the Omnibus Order change, any party may request further relief from this Court for good cause based on facts that are not currently before this Court.

b. Unblocking the Blocked Account

Based on the record before the Court, Debtor's request for authority to unblock the Blocked Account is denied through December 14, 2007. On December 7, 2007 at 10:00 a.m., the Court will hold a further hearing on whether to unblock the Blocked Account as of December 14, 2007. Any party may request that the Blocked Account be unblocked prior to that time for good cause based on facts that are not currently before this Court.

Debtor concedes that pursuant to Debtor's projected budgets, Debtor does not need to use the funds in the Blocked Account until

December 14, 2007. In reviewing Debtor's budget, Debtor projects incurring litigation expenses related to the Florida Action, in the amount of $333,333 for each week ending November 2, 2007, December 7, 2007, and January 4, 2008. This Court has stayed the Enforcement Action against FTC through March 14, 2008, and the Eleventh Circuit has stayed the Clarification Order. The Eleventh Circuit Stay Order effectively reinstates the Florida Court's September 20, 2007 order stating that the automatic stay applies to all aspects of the Florida Action, and so the Stay Order stays all other proceedings against Debtor in the Florida Action. Thus, unless this Court's order is overturned, the $666,666 that Debtor projects to spend in legal fees for the Florida Action between November 2, 2007 and December 7, 2007 is moot. Adding those funds back into Debtor's budget means that Debtor should have sufficient cash flow until the week ending December 21, 2007.

However, that is not the end of the analysis. It is this Court's understanding that part of the reason that Debtor's budget indicates that Debtor will have insufficient cash flow as of the week ending December 21, 2007 is based on Debtor's new post-petition practice of holding funds equivalent to post-petition collected and unremitted funds owed to customers. Adding the projected legal fees back into Debtor's pre-petition settlement cash balance and retaining all other assumptions, Debtor will have a deficit of $167,962 in funds held related to Debtor's obligations to customers for collected and unremitted funds for the week ending December 21, 2007 and a deficit of $185,556 in such funds for the week ending December 28, 2007. After that time, Debtor's projections indicate that Debtor will have sufficient funds to

cover Debtor's new post-petition practice of holding such funds. If this Court's understanding is incorrect or Debtor needs to use those funds, Debtor can always request further relief from this Court for good cause based on facts that are not currently before this Court or if Debtor believes the Court misunderstands the facts before it.

The Court acknowledges Debtor's new commitment to addressing an issue that resulted in Debtor's bankruptcy filing, namely Debtor's pre-petition use of funds withheld during the settlement process for Debtor's general operating expenses. Thus, on the balance sheet it appears that Debtor would have a deficit. However, it appears possible that Debtor would for two weeks have a deficit of less than $200,000 in an account that holds funds to be paid to customers at a later time. If that were true, would there be a sufficient basis for this Court to unblock the over $1.7 million in funds held in the Blocked Account to provide a reserve of less than $200,000 in case Debtor were required to remit unremitted funds to customers? By December 7, 2007, the Court and all parties will have several more weeks of actual post-petition financial information from Debtor, so a more accurate assessment of Debtor's actual need for the funds in the Blocked Account can be made. In any event, as noted above, should Debtor need the partial or full use of the funds in the Blocked Account for a period of time, the Court will consider such a request at the December 7, 2007 hearing. Moreover, should Debtor need use of the funds in the Blocked Account prior to the December 7, 2007 hearing, Debtor may request such relief before that hearing.

CONCLUSION

For the foregoing reasons, the Enforcement Action against Debtor is enjoined through March 14, 2008. On March 7, 2008 at 1:00 p.m., the Court will hold a further hearing on whether the preliminary injunction of the Enforcement Action should be continued beyond March 14, 2008. Any supplemental papers in support of continuing the preliminary injunction of the Enforcement Action after March 14, 2008 shall be filed and served by February 22, 2008. Any opposition shall be filed by February 29, 2008. Either FTC or Debtor may request that the preliminary injunction be lifted before March 7, 2008 for good cause based on facts that are not currently before this Court.

Based on the Stay Order, this Court will deny without prejudice Debtor's request for a preliminary injunction of the enforcement of the Omnibus Order. Should there currently be no such stay or should the status of a stay of the enforcement of the Omnibus Order change, any party may request further relief from this Court for good cause based on facts that are not currently before this Court.

Debtor's request for authority to unblock the Blocked Account is denied through December 14, 2007. On December 7, 2007 at 10:00 a.m., the Court will hold a further hearing on whether to unblock the Blocked Account as of December 14, 2007. Any supplemental papers in support of unblocking the Blocked Account at that time shall be filed and served by November 27, 2007. Any opposition shall be filed by December 3, 2007. Any party may request that the Blocked Account be unblocked prior to that time

for good cause based on facts that are not currently before this Court.

Counsel for Debtor shall submit a form of order consistent with this decision after review by FTC and Receiver as to form.

Dated: November 2, 2007

ARTHUR S. WEISSBRODT
UNITED STATES BANKRUPTCY JUDGE

UNITED STATES BANKRUPTCY COURT
For The Northern District Of California

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